

I thank you for this opportunity to offer comments and suggestions regarding the Proposed Rule under file no. S7-29-22: Disclosure of Order Execution Information.

I strongly support the Commission's expansion of Rule 605's scope to apply the reporting requirements to broker-dealers beyond market centers. One EMSAC committee member previously stated that retail brokerage firms would argue that "aggregate statistics are more important for retail investors" and also claimed that "[retail investors] are not going to look at the Rule 605 reports." As a retail investor myself, I can assure the Commission that this is not the case. Current statistical information required by Rule 605 alone does not provide a reliable basis to address whether any particular broker-dealer obtained the most favorable terms in execution quality under the circumstances for customer orders.

Likewise, the current aggregate statistics do not allow market participants or other interested parties to conduct their own analysis based on alternative categorizations of the underlying data and do not encompass all of the factors that may be important in evaluating the execution quality that broker-dealers obtain at a particular execution venue. Therefore, they are not as useful as they could be.

In that respect, having access to execution quality statistics, e.g. stock-by-stock order execution information specific to broker-dealers, would unquestionably be useful. It would enhance retail confidence in broker-dealers that are meeting their obligations in providing best execution of investors' orders, as well as facilitate the broker-dealers' and the Commission's ability to closely and rigorously review and analyze Rule 605 statistics as part of their legal duty and best execution compliance.

Reporting requirements of Rule 605

The Commission should require all broker-dealers to report pursuant to Rule 605, regardless of any condition or selected threshold, and should not be subjected to a de minimis order flow exclusion as described in 17 CFR 242.606(b)(3)¹.

According to the analysis presented in the Proposal, indicating "that approximately 85 broker-dealers (or approximately 6.7% of customer-carrying broker-dealers) introduce or carry more than 100,000 customer accounts" and "together handle over 98% of customer accounts", not requiring disclosures from other broker-dealers representing approximately 93.3% raises concerns about further concentration and funneling of customer order flow among a small portion of broker-dealers. This would be analogous to the asymmetrical distribution of the share of total PFOF disbursed to broker-

¹ The Electronic Code of Federal Regulations, *242.606 Disclosure of order routing information*. (November 19, 2018), [https://www.ecfr.gov/current/title-17/chapter-II/part-242/subject-group-ECFRac68bdd026a46db/section-242.606#p-242.606\(b\)\(3\)](https://www.ecfr.gov/current/title-17/chapter-II/part-242/subject-group-ECFRac68bdd026a46db/section-242.606#p-242.606(b)(3)).

dealers, or the top-heavy profit margins earned, 44% and 41% respectively, by the two largest wholesalers in terms of volume.

“Since the late 1990s, over 75% of US industries have experienced an increase in concentration levels. [...] These findings demonstrate that firms in concentrated industries are becoming more profitable predominantly through higher profit margins, rather than via greater efficiency.”²

What should be sought through the proposed Rule and by the Commission is the promotion of competition amongst all broker-dealers and market centers on the basis of execution quality. Notwithstanding the Commission’s argument stating that “a lower customer account threshold would result in capturing only marginally more customer accounts.”, it is important to look beyond customer account coverage and into the current distribution of customer accounts and retail order flow across all customer-carrying broker-dealers.

The Commission’s analysis provided in the Order Competition Rule Table 16 indicates that the top five broker-dealers received at least 2.9 times more in PFOF from NMS stocks than other broker-dealers in Q1 2022. While this does not directly measure the distribution of retail order flow across all broker-dealers, it may imply that, combined, they routed more NMS stock orders to wholesalers than the overwhelming majority. How can we call this a fair competition when 93.3% of broker-dealers cover 1.5% of customer accounts and only a small portion of retail orders?

Additionally, the Commission is basing Rule 605(a)(7) on a landscape that currently favors larger broker-dealers, given that they cover the largest amount of customers, and exclude the possibility of lowering the discrepancy in terms of retail order flow volume between smaller and larger broker-dealers. Providing execution quality reports constitute a significant advantage because they would be relevant to retail investors and could be a tipping point in their decision to part away with their current broker-dealer.

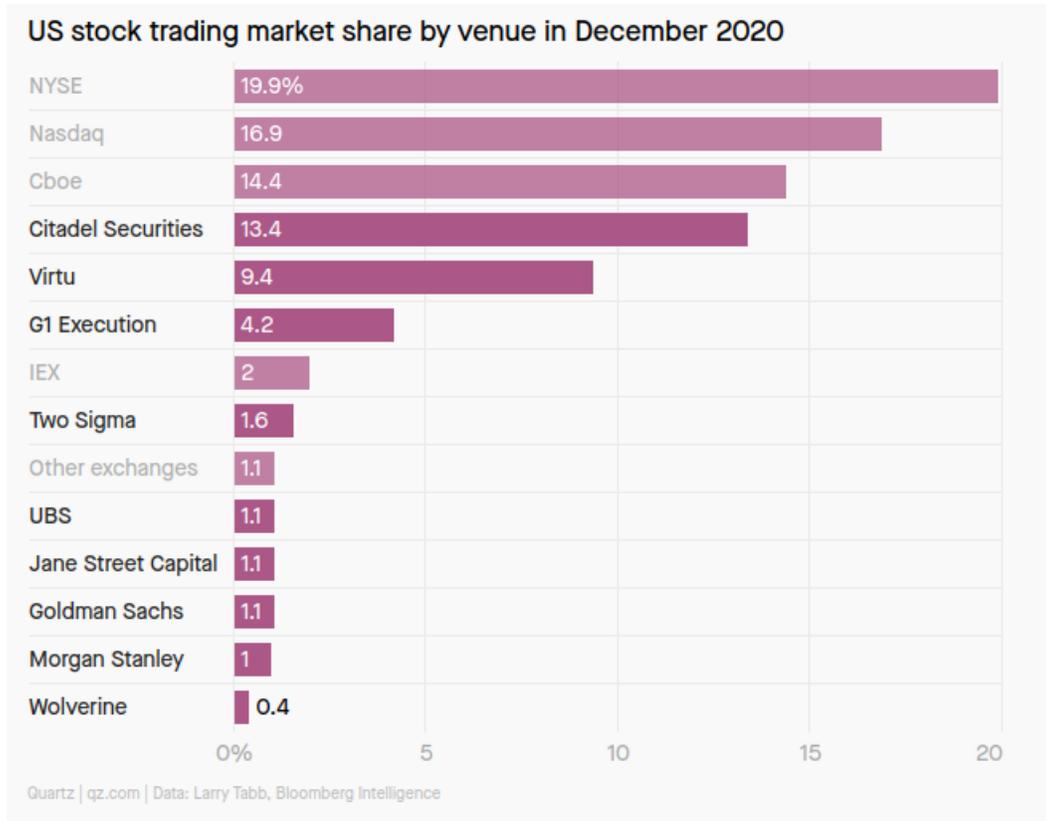
Transparency is key in attracting and retaining retail customers, as seen in recent market events where they will switch broker-dealers or exit brokerages altogether, opting for transfer agents instead when requested transparency isn’t provided, or when their broker-dealer performs nontransparent actions misaligned and incongruent with their customers’ interests, e.g. position closing only (PCO) trading restrictions³.

In a hypothetical scenario, would the market be better off if smaller wholesalers were exempt from disclosure requirements due to their limited bargaining power in relation to larger wholesalers in terms of payment relationship and arrangements with broker-dealers (PFOF), receiving a smaller share of

2 Gustavo Grullon, Yelena Larkin, Roni Michaely, Are US Industries Becoming More Concentrated?, *Review of Finance*, Volume 23, Issue 4, July 2019, Pages 697–743, <https://doi.org/10.1093/rof/rfz007>.

3 McCabe, Caitlin, *Robinhood, Other Brokerages Restrict Trading on GameStop, AMC*, *The Wall Street Journal*. Dow Jones & Company. (January 28, 2021), <https://www.wsj.com/articles/online-brokerages-restrict-trading-on-gamestop-amc-amid-frenetic-trading-11611849934>.

NMS stock orders, having a smaller percentage of overall trading volume⁴, and therefore earning lower profit margins? In the interest of transparency, would it be appropriate to exclude these wholesalers based on certain criteria or thresholds given the oligopsony landscape?



Likewise, if retail investors were forced to route their orders directly to wholesalers in a hypothetical dystopian scenario, and only larger wholesalers were required to provide, for instance, execution quality reports on internalized orders, which wholesaler does the Commission believe they would pick: larger, transparent wholesalers or smaller, nontransparent ones? The answer is quite obvious, similar to how retail investors desire their orders to be sent directly to lit exchanges rather than off-exchange, to wholesalers, or to dark markets.

Considering that there are 1267 broker-dealers according to Table 12 of this Proposal, competition amongst all broker-dealers would be stifled even further. Under proposed Rule 605, the future landscape could result in “some smaller broker-dealers to exit the market” as the Commission suggested, because they may not be willing or able to provide similar execution quality reports, or they may be unable to afford those costs, and therefore lose customers, prompting their exit. In that regard, requiring all broker-dealers to report pursuant to Rule 605 may cause them to exit the market anyway.

⁴ Detrixhe, John, *Citadel Securities gets almost as much trading volume as Nasdaq*, Quartz. (February 5, 2021), <https://qz.com/1969196/citadel-securities-gets-almost-as-much-trading-volume-as-nasdaq>.

Unfortunately, that is the reality and nature of competition. While this would indeed present a barrier to entry for smaller broker-dealers in its initial costs estimated at \$37,020 per respondent, and ongoing costs that in theory would be mitigated by computational scalability of order volume or third-party vendors and thus present varying costs for reporting entities, transparency ought to be prioritized and put at the forefront of the proposed Rule. For instance, if a broker-dealer receives zero held orders, typically used by individual investors, and is required to produce Rule 605 reports which “only contain information about the execution quality of investors’ held orders”, then would it realistically introduce ongoing costs totaling an annual monetized burden of \$37,488? I truly hope not. Transparency must be the bare minimum for any broker-dealer or market center from the outset.

Furthermore, the Commission mentioned that it “does not believe this [if some smaller broker-dealers were to exit] would significantly impact competition in the market for brokerage services because the market is served by a large number of broker-dealers.” I wonder, then, why not require all broker-dealers to report pursuant to Rule 605? Even if some smaller broker-dealers were to exit, or even if it would marginally increase the number of smaller broker-dealers exiting under my suggestion, the market would still be served by a large number of broker-dealers according to the Commission, while providing transparency to all market participants and other interested parties. It would also enable investors, third-party analysts, and academic researchers to examine the extent to which smaller broker-dealers may innovate and compete to provide similar or better execution quality than larger broker-dealers in order to attract retail investors, potentially leading to their business models adapting and expanding to serve new customers who may have previously been primarily comprised of institutional investors. Requiring all broker-dealers to report under Rule 605 would provide a level playing field for smaller broker-dealers to differentiate themselves and fill any gaps in unsatisfactory, insufficient, or inadequate service left by larger broker-dealers.

Besides, this would simplify and streamline the Proposal by eliminating the need for a “grace period”.

Moreover, retail investors served by broker-dealers excluded from this proposed Rule should not be disadvantaged. It would be unfair to them to be at the mercy of their broker-dealer’s willingness to provide execution quality reports in the scenario that they are not required, and subsequently be forced to switch from a smaller broker-dealer that they may prefer to a larger broker-dealer, which would result in less competition amongst all customer-carrying broker-dealers and the aforementioned funneling.

The absence of these reports would represent a barrier to entry for retail investors in doing business with smaller broker-dealers. Accordingly, execution quality reports would become a major factor in weighing different broker-dealers, and having fewer choices would adversely reduce competition.

“Competition in America is about price, selection, and service. It benefits consumers by keeping prices low and the quality and choice of goods and services high. Competition also encourages businesses to offer new and better products.”⁵

Under this proposed Rule, smaller broker-dealers would immediately be eliminated as options for many investors, as their choices would be significantly reduced and limited to those disclosing execution quality information, regardless of other factors such as the availability of customer support, the quality of customer service, the handling of orders during volatile or downward-trending market conditions, the user interface, the user experience, etc. This is solely because they do not provide comparable execution quality information on a stock-by-stock basis or summary reports with aggregated execution quality information. For any reasonable justification that they may express, such as wanting to save on the initial and ongoing costs of Rule 605’s reporting requirements, it does not inspire confidence or deserve the unequivocal trust of retail investors in their legal duty to comply with best execution of customer orders.

"The national market system objectives of section 11A of the Exchange Act include the economically efficient executions of securities transactions; fair competition among brokers and dealers, among exchange markets, and between exchange markets and markets other than exchange markets; the availability of information on securities quotations and transactions; and the practicability of brokers executing investor orders in the best market."⁶

Reporting requirements for only 6.7% of broker-dealers does not constitute transparency or promote fair competition. It conversely conceals execution quality information and best execution compliance, secludes competition in favor of larger broker-dealers, and certainly fails to meet the NMS objective of “availability of information on securities transactions” by precluding retail investors’ ability to access execution quality reports within smaller broker-dealers.

Although Rule 605 reports may not be necessary for institutional investors who conduct their own analysis of execution quality or obtain it from third-party vendors, e.g. transaction cost analysis (TCA) of their orders, requiring all broker-dealers to report under Rule 605 could help smaller broker-dealers attract retail investors, increase revenue, and elevate competition. This could involve offering improved service or implementing new features that could also be beneficial to institutional investors.

Broker-dealers and market centers that are subject to Rule 605’s reporting requirements should also be required to provide a summary report reflecting aggregated execution quality information. It is in the best interest for competition to enable individual investors to quickly assess comparable and digestible statistical reports. Fostering healthy competition on the basis of execution quality requires accessibility

5 Federal Trade Commission, *Competition counts: How consumers win when businesses compete*. https://www.ftc.gov/system/files/attachments/competition-counts/pdf-0116_competition-counts.pdf.

6 Securities and Exchange Commission, *Order Competition Rule*. (December 14, 2022), <https://www.sec.gov/rules/proposed/2022/34-96495.pdf>.

and transparency for all market participants. Not all individual investors may have the time or the ability to collect and analyze stock-by-stock order execution information, and might only be interested in examining or comparing the overall execution quality of specific broker-dealers and market centers.

Market centers operating qualified auctions should indeed provide price improvement statistics for segmented orders. These additional metrics would provide valuable information to individual investors based on regularly-used execution venues to which specific broker-dealers may route orders, as indicated in Rule 606 disclosures. As a result, individual investors who choose to switch broker-dealers, given that information, may influence broker-dealers' order routing decisions when exposing individual investor orders to qualified auctions, and ultimately drive higher competition among qualified auctions at different market centers in providing better price improvement for segmented orders.

In accordance with the Regulation NMS definition of "time of order receipt", a broker-dealer that is not a market center should be mandated to calculate the time of order receipt using the same criterion, namely, when the order was received by the broker-dealer for execution. For instance, when a customer places an order at a restaurant, they anticipate that the food delivery process will commence once the order has been completed and received by the waiter or waitress. The best execution of the order is then exclusively reliant on the restaurant's ability to execute it effectively. If the execution of an order were calculated using the time the order was sent to the kitchen staff instead, it would not take into account any delays between the time the customer placed the order and the receipt of the order by the waiter or waitress. This would imply that a one-hour delay or more would be deemed acceptable.

I fully support the Proposal to require broker-dealers operating alternative trading systems ("ATs") or single-dealer platforms ("SDPs") to provide separate reports for orders in connection with other trading activity of its broker-dealer operator, as outlined in Rule 605. This will enhance transparency by enabling clear and distinct reporting of each entity's activity. Mixing information from different entities in a single report can introduce noise and hinder the ability to discern differences in execution quality. By requiring separate reports, it will be easier to compare the execution quality statistics of different reporting entities and ensure that the information provided is accurate and meaningful.

Centralized electronic system

I commend the Commission for its thoughtfulness and foresight in recognizing the EDGAR alternative system, which does not contemplate filing Rule 605 information with the Commission. While this would have been, for the most part, the ideal solution for a centralized electronic system for Rule 605 reports, the implementation of such a system must not compromise or weaken the liability for misstatements contained in documents similar to those furnished to the Commission. This may increase reporting entities' nonchalance towards compliance with proper disclosure requirements, which is

already an existing issue⁷. The Division of Examinations reported on November 10, 2022, that improper, inaccurate, and missing disclosures were observed, particularly with regards to firms' quantifiable disclosures and material aspect disclosures related to broker-dealers' compliance with Regulation NMS Rule 606 disclosure requirements.

Nonetheless, I recommend that the Commission require Rule 605 reports to be posted in a centralized location, implemented in a way that does not restrict the liability for misstatements. While I agree with the benefits that the Commission has listed for a centralized electronic system, I want to emphasize the aspect of accessibility and ease of navigation. With so many broker-dealers being required to report under Rule 605 on their websites, the task of searching can be daunting and time-consuming. A single centralized location will significantly improve market participants' data collection and aggregation process, and it is likely to increase market participants' involvement in seeking Rule 605 reports, including downloads, as competition will in part revolve around execution quality.

It is essential to ensure that these reports are appropriately standardized, formatted, and completed before acceptance through programmatic checks. This will facilitate comparability and eliminate the burden of maintaining a software tool that is at risk of format changes, file relocation, etc. The benefits clearly outweigh any drawbacks, and the lack of a centralized electronic system for Rule 605 reports would limit these benefits and proposed amendments. Hence, I suggest that the Commission require both summary and detailed reports to be posted in a centralized location, ideally a centralized electronic system implemented by the Commission and subjecting reporting entities to liabilities, with no access fees charged to anyone. Summary reports reflecting aggregated execution quality information would be more digestible for most investors, while detailed reports would be preferred by market participants willing to process and analyze these disclosures based on their categorization of the underlying data. Therefore, having both types of reports in a single location will help improve accessibility and lower search costs.

Overall, I firmly believe that this Proposal will increase long overdue and needed transparency, although I hope the Commission considers my points regarding reporting requirements for all broker-dealers. In conjunction with other proposed Rules, it will significantly improve and promote competition on the basis of execution quality.

Finally, I want to express my support for this Proposal.

Sincerely,

J. T.

⁷ The Division of Examinations, *Observations Related to Regulation NMS Rule 606 Disclosures*. (November 10, 2022), <https://www.sec.gov/files/reg-nms-rule-606-disclosures-risk-alert.pdf>.